IN THE SUPREME COURT OF THE STATE OF DELAWARE

IN RE PINPOINT BEARINGS, INC. SHAREHOLDERS LITIGATION	)	No. 17, 2011

EDWARD MILLER, Plaintiff Below-Appellant, v. MICHAEL SANCHEZ, CLARE MITCHELL, BRENDAN ELLSWORTH, TIMOTHY FLETCHER, MARSHA FRANKLIN, DAPHNE KEYES AND ERIC LAM, Defendants Below-Appellees, and PINPOINT BEARINGS, INC., Nominal Defendant Below-Appellee.	)	Court Below: Court of Chancery of the State of Delaware in and for New Castle County Civil Action No. 4958 VCM

Plaintiff's Interlocutory Appeal

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NATURE OF THE PROCEEDINGS

On December 1, 2010, Edward Miller ("Miller") filed a Federal Action against the directors of Pinpoint Bearings, Inc. ("the Board") in the United States District Court for the Southern District of Texas ("S.D. Tex."). Miller alleges the Board breached their corporate fiduciary duties under Delaware law and is in violation of Federal Securities law. The next day, three other Pinpoint shareholders filed similar fiduciary complaints against the Board in Delaware. Shortly thereafter, Miller filled his own Delaware compliant and moved to have his complaint consolidated with the other three Pinpoint shareholders (the consolidated action). Then, Miller, as a member of the Delaware proceeding, requested that the Court of Chancery stay the consolidated action in favor of the proceedings in Texas. (R. at 9.) The court consolidated the four cases, but denied Mr. Millers' motion to stay proceedings in Delaware. Further, the court enjoined Mr. Miller from prosecuting the state law derivative claims in Texas. (R. at 20-21.)

Mr. Miller filed a certification of interlocutory appeal in accordance with Supr. Ct. R. 42 and asked this Court for a hearing to review his case *de novo*. (Order 2, Appeal 1-2.) Therefore, this Court has jurisdiction to accept Mr. Miller's appeal under Supr. Ct. R. 42 and review his final judgment under Del. Const. art. IV, § 11 (2011). (Appeal 2.)

SUMMARY OF ARGUMENT

Mr. Mill presents three arguments in support of this action. First, the exclusive forum provision is invalid as it was improperly adopted by the Board. The exclusive forum provision substantially limits shareholders rights, and as such, can only be adopted through a charter amendment. Section 109(b) of the Delaware General Corporation Law (DGCL) states that bylaws may only contain provisions that **relate** to the rights of the shareholders; whereas Section 102(b)(1) states that provisions **limiting** shareholder rights

may be adopted through a charter amendment, which is subject to a shareholder vote. Therefore the board of directors failed to properly adopt the exclusive forum provision.

Second, the exclusive forum bylaw again violates Section 109(b). Section 109(b) proscribes the adoption of bylaws that are contrary to law. Under the United States Supreme Court's "unjust and unreasonable" test the exclusive bylaw appears to be contrary to law and therefore, in violation of Section 109 (b).

Third, the Board violated its fiduciary duty of loyalty by unilaterally amending the bylaws of Pinpoint. The Court of Chancery incorrectly applied the business judgment rule when it examined the exclusive forum selection bylaw. Under *Blasius'* compelling justification standard of judicial review, the Board, in acting unilaterally, needed to provide compelling reasons to support its dismissal of the shareholder vote. The Boards arguments of convenience, predictability of judicial decisions, and efficiency are not enough to overcome the heavy burden of proving the decision was justified. The fiduciary duty of loyalty owed to the shareholders was violated through the unilateral amendment to the bylaws.

Finally, Miller's Motion to stay proceedings in Delaware should be granted. The facts and circumstances of this case show that staying proceedings in Delaware, in favor of Texas, is proper under both a *McWane* and *Forum Non Conveniens* analysis.

STATEMENT OF FACTS

For purposes of this appeal, the following facts are undisputed. Appellant, Mr. Miller, is a lifelong resident of Texas and current shareholder of Pinpoint Bearings, Inc. ("Pinpoint"). Pinpoint is a Delaware

corporation with its corporate headquarters and manufacturing operations in Houston, Texas. (R. at 3-4.) Mr. Miller currently owns 5,000 shares of Pinpoint common stock worth $230,000. (R. at 3.) Most of Mr. Miller's shares in Pinpoint were acquired during his twenty year service at Pinpoint, from 1984 to 2004. (R. at 3-4.) The remaining shares were acquired from 2009 to 2010. (R. at 3.)

Pinpoint specializes in manufacturing engineered precision roller and ball bearings for aerospace application. (R. at 4.) Its principal customer is the U.S. military ("USM"), who accounted for more than 60% of Pinpoint's annual revenues over the last five years. (R. at 4-5.) Each USM-Pinpoint contract requires that Pinpoint comply with a variety of performance and safety stress tests before shipping the bearings. (R. at 5.) The contracts further require that Pinpoint certify in all billings and invoices that it performed the tests and the tests were satisfactory. *Id.*

In early 2009, Roland Thompson ("Thompson"), a Pinpoint employee, discovered three mid-level managers at Pinpoint did not test the military aircraft bearings regularly. *Id.* Thompson further discovered that Pinpoint falsely misrepresented to the USM that it performed the tests and the tests were satisfactory. *Id.* A year later, Thompson contacted the Office of the Inspector General of the United States ("OIG") concerning a pattern of improper cost cutting measures in the USM-Pinpoint contracts. (R. at 6.) Because of this, the government launched an official investigation and informed the Pinpoint Board of its investigation. *Id.*

On June 10, 2010, the Pinpoint Board adopted a forum bylaw, giving the Court of Chancery an exclusive right to hear any derivative claims against or on behalf of Pinpoint. (R. at 2.)

On September 10, 2010, Pinpoint CEO, Michael Sanchez, called a meeting of the Board and appointed two independent directors to a special investigation committee ("Special Committee"). (R. at 6.) Sanchez then hired the Houston law firm of Venner and Lee as outside counsel to aid the investigation. *Id.* The Special Committee and the Houston firm confirmed the truth of Thompson's complaint, and with the Board's approval, the Houston firm negotiated a settlement with the OIG on November 30. *Id.* Immediately after the finalization of the OIG-Pinpoint settlement, the Pinpoint Board issued a press release disclosing the investigation and the settlement. (R. at 7.)

The next day, Mr. Miller filed a Federal Action against the Board in the United States District for the Southern District of Texas ("S.D. Tex."). *Id.* His complaint explained that the Board failed to create or maintain a compliance system, to ensure the USM-Pinpoint contract was met. This failure by the Board is a breach of its fiduciary duty of oversight. (R. at 5.)

Three Pinpoint shareholders filed identical state fiduciary claims in Delaware. (R. at 7.) On December 6, the three shareholders submitted a proposal to the Delaware Court of Chancery ("Court of Chancery") to consolidate their complaints ("Original Delaware Actions"). (R. at 8.) The Court of Chancery entered the proposal on December 8. *Id.*

The Pinpoint Board then filed a motion in the S.D. Tex. to keep the Original Delaware Actions in Delaware. *Id.* Mr. Miller responded by filing a second action ("Miller Delaware Action") that alleged the same complaint as his Federal Action. Id. Mr. Miller then requested that the Miller Delaware Action be consolidated with the Original Delaware Actions. (R. at 9.) Simultaneously, Mr. Miller asked the court to stay the Miller Delaware Action and the Original Delaware Actions ("Delaware Motion to Stay") in favor of the Federal claim in Texas. *Id.*

Included in his Delaware Motion to Stay, Mr. Miller requested that the Court of Chancery find the board-adopted forum bylaw to be invalid as a matter of Delaware law. *Id.* Pinpoint's Board opposed Mr. Miller's Motion to Stay and asked the Court of Chancery to bar Mr. Miller from prosecuting any derivative claims against the Board in a forum outside Delaware. (R. at 10.) The court granted the Board's request. Mr. Miller responded, asking the Delaware Supreme Court for a hearing to review his claim, invalidate the board-adopted forum bylaw, and allow him to litigate the Original Delaware Actions with his Federal Action in the S.D. Tex. (Appeal 2.)

ARGUMENT

I. SCOPE OF REVIEW

This Court should review the decision of the Court of Chancery *de novo*. *De novo* review typically requires courts to review the meaning or application of a controlling law, then, address the issues as if they have not been decided. *Brehm v. Eisner*, 746 A.2d 244 (Del. 2000). The facts in claims reviewed *de novo* are generally agreed upon and, thus, the reviewing court focuses on whether the undisputed facts meet the disputed legal standards. *Id.* In deciding the issues, the reviewing court must not defer to any findings made by the court below. Rather, the reviewing court must substitute its judgment for that of the previous court. *Rohner v. Niemann*, 380 A.2d 549 (Del. 1977); *Fiduciary Trust Co. of N.Y. v. Fiduciary Trust Co. of N.Y.*, 445 A.2d 927 (Del. 1982).

II. IS THE UNILATERAL ADOPTION OF AN EXCLUSIVE FORUM BYLAW BY THE BOARD OF DIRECTORS WITHOUT SHAREHOLDER CONSENT VALID UNDER DELAWARE LAW?

A. Standard

"Bylaws which are contrary to statute or law are void."[1] "The bylaws of a corporation are presumed to be valid and are to be construed in a manner consistent with law."[2] Therefore the burden is on the party opposing the enforcement of the bylaw to show its invalidity. Further, bylaws must be *reasonable* in their application.[3]

B. The Exclusive Forum Provision Substantially Limits Shareholder Rights and Therefore Can Only Be Properly Adopted Through a Charter Amendment Subject to a Shareholder Vote

The shareholders' "right to pursue effective enforcement of the fiduciary duties owed to them, as defined by corporate law, is a fundamental one."[4] Section 109(b) of the DGCL states that the bylaws of a Delaware corporation may contain "any provision… **relating** to the … powers of its stockholders, directors, officers or employees."[5]

Section 109(b) essentially defines bylaws as procedural mechanisms through which the shareholders and directors can determine how the company will operate. However, when determining the powers of directors and shareholders in a company, 8 Del. C. § 102(b)(1)controls. Section 102(b)(1) states that the charter can contain provisions "creating, defining, limiting, and regulating the powers of the corporation, the directors, and the stockholders."[6] Therefore, only a charter can contain provisions that limit shareholder rights.

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[1] 8 W. Fletcher, *Cyclopedia of the Law of Corporations* § 4176 (rev. perm. ed. 1982).
[2] *Frantz Mfg. Co. v. EAC Indus.*, 501 A.2d 401, 407 (Del. 1985).
[3] *Schnell v. Chris-Craft Industries, Inc.*, Del.Supr., 285 A.2d 437 (1971).
[4] Stevelman, Faith, *Regulatory Competition, Choice of Forum, and Delaware's Stake in Corporate Law* at 39 (April 29, 2009); *See also Siegman v. Tri-Star Pictures, Inc.*, Del. Ch., C.A. No. 9477 (May 5 , 1989).
[5] Del.Code Ann. tit. 8, § 109(b)(2001)(emphasis added).
[6] 8 Del. C. § 102(b)(1).

C. The Exclusive Forum Bylaw is Unjust and Unreasonable in its Application and Therefore Violates Federal Law and Section 109(b) of the DGCL

Exclusive forum provisions are invalid if it can be shown that their application would be unjust or unreasonable.[7] Forum selection provisions are also subject to judicial scrutiny for fundamental fairness.[8] Some legal scholars believe judicial scrutiny is even more appropriate where the exclusive forum provision is adopted by directors through a bylaw -- reasoning that specific method was chosen to avoid adopting it through a charter amendment, which would be subject to shareholder vote.[9]

Section 109(b) of the DGCL states that the bylaws of a Delaware corporation may contain "any provision, **not inconsistent with law**…"[10] In the context of the current case, the bylaw is both unjust and unreasonable and therefore violates both federal law and Section 109(b) requirement that a bylaw not be inconsistent with the law.

The United States Supreme Court looked at four factors in determining whether an exclusive forum provision was invalid, each of which being sufficient by itself to determine the provisions validity. Two of those four factors are relevant in the current action. Those factors are whether the forum selection provision: (1) was the product of fraud or overreaching and (2) was "freely negotiated." Each of these factors is considered below.

1. The Exclusive Forum Bylaw Was the Product of Overreaching by The Board of Directors

Courts will not enforce a forum selection provision that was procured through overreaching.[11] In *Carnival Cruise Lines v. Shute*, 499 U.S. 585, 595

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[7] *The Bremen v. Zapata Off-Shore Co.*, 407 U.S. 1 (1972).
[8] *Carnival Cruise Lines v. Shute*, 499 U.S. 585, 586 (1991).
[9] Davidoff, Steven, *A Litigation Plan That Would Favor Delaware*, N.Y. Times (October 26, 2010).

[10] Del.Code Ann. tit. 8, § 109(b)(emphasis added).
[11] *M/S Bremen v. Zapata Off-Shore Co*., 407 U.S. 1, 12-13, 15 (1972).

(1991) the Supreme Court held that a Florida forum selection provision incorporated into a cruise ticket was valid and enforceable. In so holding, the Supreme Court reasoned that "there was no indication that [the] cruise line set Florida as [the] forum as a means of discouraging cruise passengers from pursuing legitimate claims.

However, in the current case, the forum selection bylaw was "adopted by the very individuals who are named as defendants…after the alleged wrongdoing took place, [where] there is no element of mutual consent to the forum choice at all."[12] The Exclusive Forum Bylaw was adopted by the Board just three months before they were notified that Pinpoint was being investigated by the federal government. The purported bylaw designated Delaware as the exclusive jurisdiction in which derivative claims could be brought.

Pinpoint has no connections with Delaware other than being incorporated there. The Board adopted the Bylaw as a means of discouraging shareholder litigation by making Delaware the exclusive forum for derivative litigation. Thus, the board has effectively burdened the process through which it could be held accountable. First, the Board has discouraged any shareholder not within the vicinity of Delaware from instituting an action. Second, it has placed the events and evidence that gave rise to its liability, here, 1,600 miles away. This is the Board abusing its powers to dictate where and how it can be sued.

2. The Exclusive Forum Bylaw Was Not "Freely Negotiated" as it was Unilaterally Adopted by the Board of Directors Without Shareholder Consent or Notice

The U.S. Supreme Court has also stated that a forum selection provision will be held unenforceable if it was not "freely negotiated."[13] This is evidenced in *Carnival Cruise Lines*, 499 U.S. 585. *Carnival* explains that just

[12] *Galaviz v. Berg*, No. 10-cv-3392, slip op. (N.D. Cal. Jan. 3, 2011).
[13] *M/S Bremen v. Zapata Off-Shore Co.*, 407 U.S. 1, 12 (1972).

because a contract was not expressly bargained for does not mean it was not "freely negotiated." The crux of the Court's decision as to whether an exclusive forum provision was valid seemed to turn on whether one party had exercised "overweening bargaining power" in the acquisition of the provision.

The Court established that the exclusive forum provision was enforceable mainly because the Plaintiff admitted to having notice of the provision and, although not expressly bargained for, took her cruise ticket subject to its terms having initially "retained the option of rejecting the contract with impunity."[14]

In the current case, however, the shareholders had no notice of the adoption of the exclusive forum bylaw and were not afforded the initial option of rejecting it. Although shareholders do have the option of amending the bylaws themselves to remove the exclusive forum bylaw, "this is extremely unlikely to happen as a practical matter because of the costs of calling and holding a shareholder meeting over such a proposal."[15]

The Court also noted that *Carnival's* bylaw established the dispute forum *ex ante* and had the "salutary effect of dispelling confusion as to where suits may be brought and defended, thereby sparing litigants time and expense and conserving judicial resources." [16] Again, the current case can be distinguished as the Board adopted the exclusive forum bylaw *ex post*; at least with respect to shareholders who purchased stock prior to the adoption. This leaves the salutary effects described above ineffectual.

The Bylaw is unenforceable as it has been shown to be unjust and unreasonable under either of the above factors.

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[14] *Carnival*, 499 U.S. at 595.
[15] *See* Davidoff.
[16] *Carnival*, 499 U.S. at 585.

III. UNDER THE BLASIUS "COMPELLING JUSTIFICATION" STANDARD DID THE PINPOINT BEARINGS BOARD OF DIRECTORS VIOLATE ITS FIDUCIARY DUTY TO THE SHAREHOLDERS BY UNILATERALLY AMENDING THE BYLAWS TO INCLUDE AN EXCLUSIVE FORUM SELECTION CLAUSE?

The Pinpoint Board breached its fiduciary duty of loyalty by unilaterally amending the bylaws to include the Exclusive Forum Bylaw. "The directors of Delaware corporations have a triad of primary fiduciary duties: due of care, loyalty, and good faith. Those fiduciary responsibilities do not operate intermittently."[17] Upon learning of a potential breach of duty, shareholders may bring an action against the board. "[G]enerally one of three standards of judicial review is applied: the traditional business judgment rule, an intermediate standard of enhanced judicial scrutiny, or the entire fairness analysis."[18] The court must determine the appropriate standard of review in light of the given facts.

A. Standard

The necessary standard of judicial review to examine the Boards actions is the Blasius "compelling justification" standard. The Board must show it had compelling reasons to interfere with the shareholder vote. Mr. Miller correctly asserts that the Court of Chancery incorrectly applied the business judgment rule when it ruled in favor of the Board.

B. The Business Judgment Rule is Not the Appropriate Standard for This Case.

The Board amended the Pinpoint bylaws in June 2010 without any formal legal consultation or shareholder vote. This unilateral action to include the Bylaw warrants a standard of review higher than the business judgment rule. "The business judgment rule is a presumption that, in making a business decision the directors of a corporation acted on an informed basis, in good faith and in the honest belief that the action taken was in best interests of

[17] *Emerald Partners v. Berlin*, 787 A.2d 85, 90 (Del. 2001).
[18] *Id*. at 89.

the company and its shareholders."[19] The Court of Chancery overlooked the board's action determining it was in good faith and in the honest belief the bylaw was in the best interest of the company and its shareholders. (R at 18.) Moreover, as previously stated, the record is devoid of any indication that the board was informed by legal counsel apart from a reference to a Director Defendant affidavit, which is not included in the record. *Id*. Further, the record provides no indication the shareholders were notified about the change.

While this is not the appropriate standard for this case, it is necessary for shareholders to assert a presumption that the board acted outside of its bounds when it took action.[20] The acknowledgment of a potential business judgment violation shifts the burden to the defendants to prove otherwise.[21] The Court of Chancery reasoned the board was not self-interested apart from wanting to have a convenient, efficient, and predictable court decide derivative suits. This presumption of disinterestedness needs to be proven by the Board.

Typically, a court will not substitute its judgment for that of a board of directors, "Unless it is shown by a preponderance of the evidence that corporate directors' decisions were primarily based on perpetuating themselves in office, or some other breach of fiduciary duty."[22] This case presents a different scenario. The year prior to the Bylaw change, Pinpoint engaged in cost cutting measures that led to the Federal Action in the Texas Court. In June 2010, without specified reason, the Board adopted the Bylaw that states any derivative action needs to be brought in the Delaware court. (R. at 3.) The Boards lack of explanation for the adoption is reason enough

[19] *Id*. at 90-91.
[20] *Id*. at 90.
[21] *Id*. at 91.
[22] *Unocal, Corp. v. Mesa Petroleum Co*., 493 A.2d 946, 958 (Del. 1985)

for the court to examine the Bylaw with a stricter standard than that of the business judgment rule.

C. The Blasius "Compelling Justification" Standard is the Proper Standard of Judicial Review.

Because this case deals with a board's interference with the shareholder vote, the Blasius "compelling justification" standard is the correct intermediate level of judicial review. According to the Blasius court, a conflict is created between the board and the shareholders when action is taken to interfere with the shareholder vote, therefore, making the business judgment rule inapplicable. *Blasius Industries, Inc. v. Atlas Corp.*, 564 A.2d 651, 659-60 (Del. Ch. 1988). The Board was under no threat at the time it unilaterally amended the bylaws. Therefore, its action should not be protected by the business judgment rule. The Boards decision to act unilaterally without the shareholder vote on an issue that primarily affects the shareholders is the type of voting issue the Blasius standard seeks to defend.

Legal scholar Gregory Schaer argues that the Blasius standard prepares a board of directors for this standard of judicial review if it restricts a shareholder vote. *Blasius Industries, Inc. v. Atlas Corp.: Closer Scrutiny of Board Decisions under the "Compelling Justification"*, 16 Del. J. Corp. L. 639, 662 (1991). This does not mean that the board action will become per se invalid upon this showing. *Blasius,* 564 A.2d at 661. Rather, the board then bears the heavy burden of showing "compelling justification" for its actions. *Id*. Through application, the Pinpoint Board must bear this heavy burden to demonstrate the compelling reasons it enlisted to unilaterally amend the bylaws. Its argument for convenience, efficiency, and judicial similarity is one the shareholders should have decided as they carry the burden of bringing

derivative suits in Delaware. The Board acted in a way to prevent the shareholders from voting on this issue.

Distinguishing the *Blasius* case, where two corporations fought over board positions, this case presents a board that overstepped its bounds to interfere with the shareholder voting right. This interference of the shareholder franchise is the type of action that calls for the compelling justification standard. Unilaterally adding the Exclusive Forum Bylaw is not a compelling justification, since the Board was not responding to a threat. This absence of urgency is enough to show that the Board did not act with good faith. Rather, it violated its fiduciary duty of loyalty. Because of this, the Bylaw is, invalid. "The only justification that can be offered for the action taken is that the board knows better than do the shareholders what is in the corporation's best interest."[23] Exclusive forum bylaws do not seem to fit into the immediacy category of a company's best interest. In *MM Co.* there was the board of Liquid Audio sought to dilute the voting strength of MM, a corporate director, by expanding the board.[24] This was seen as an inappropriate amendment to the bylaws.[25] Here, the Board is eliminating the strength of the shareholders to vote on issues primarily affecting them and eliminating their ability to bring derivative suits in courts of competent jurisdiction. The Bylaw's primary purpose is to shield the Board from being subject to jurisdiction in many different states; a self-interest justification.

While the Court of Chancery examined the Board's action under a Unocal and Unitrin standard, those are not applicable here. Unocal and Unitrin

[23] *MM Co., Inc. V. Liquid Audio, Inc.*, 813 A.2d 1118, 1129 (Del. 2003).
[24] *Id*.
[25] *Id*.

protect defensive measures when faced with a takeover.[26] The Blasius compelling justification rests in each of those standards, but it may also act independently when a Board is not faced with "a hostile contest for control." *Id*. Not faced with a takeover situation, the Board's unilateral action only requires the compelling justification standard of judicial review.

As explained in Sections II and III above, this Court should also find the bylaw invalid and unenforceable because it: (1) is contrary to Delaware law, (2) is unjust and unreasonable, (3) is the product of overreaching by the Board, and (4) interferes with the shareholders vote without a compelling justification to do so.

The exclusive forum provision is invalid and cannot be considered a contract between Mr. Miller and the company. Therefore it cannot be said that Mr. Miller contracted away his right to bring suit in a proper forum of his choosing. Both Texas and Delaware are Courts of competent jurisdiction in this case. Therefore this Court must now determine whether it should stay the Delaware proceedings in favor of the proceedings in Texas. In determining if a stay of proceedings is appropriate, Delaware Courts have applied the standards and processes discussed immediately *infra* in Section IV.

IV. THE DELAWARE PROCEEDINGS CAN AND SHOULD BE STAYED IN FAVOR OF THE PROCEEDINGS IN TEXAS UNDER BOTH THE MCWANE DOCTRINE AND A FORUM NON CONVENIENS ANALYSIS

A. Standard

"The granting of a motion to stay is not a matter of right, but rather rests within the sound discretion of the court.[27] The threshold issue when

[26] *Id*. at 1130

[27] *Rapaport v. The Litig. Trust of MDIP Inc*., 2005 WL 3277911, at *2 (Del. Ch. Nov. 23, 2005)(*citing McWane Cast Iron Pipe Corp. v. McDowell-Wellman Engineering Co*., 263 A.2d 281 (Del. 1970)

deciding whether to stay an action in this Court in favor of an action pending elsewhere is which action was filed first. If the action in this Court is the first-filed action, '[Delaware] courts will uphold a plaintiff's choice of forum except in the rare case where that choice imposes overwhelming hardship on the defendant.'"[28]

If the foreign action is the first-filed action, 'principles of fairness, comity, judicial economy and the possibility of inconsistent results generally favor the granting of a stay.' [29] If the actions were contemporaneously filed, our courts will evaluate a motion for a stay 'under the traditional *forum non conveniens* framework without regard to a *McWane*-type preference of one action over the other.'"[30]

B. The Court Should Apply the McWane Doctrine in Determining Whether to Stay the Delaware Proceedings as the Foreign Action Was First Filed

In deciding the appropriate forum for litigation where similar actions are pending in two separate forums, Delaware Courts will apply one of two frameworks: (1) a *Forum Non Conveniens* analysis or (2) the *McWane* Doctrine. In determining which framework to use, the Court must decide which action was first filed.

In a conventional *McWane* analysis (where a Plaintiff and Defendant have filed similar actions in competing forums) Delaware Courts look primarily to which action was filed first. Delaware court will typically stay proceedings in Delaware so long as the foreign action has: (1) the same parties, (2) the same issues, and (3) a court capable of providing prompt and complete justice.

However, in the context of a forum dispute between two derivative plaintiffs who have filed actions in separate forums, the Delaware Chancery

[28] *Id.* (*citing United Phosphorus, Ltd. v. Micro-Flo, LLC*, 808 A.2d 761, 764 (Del.2002).
[29] *Id*. (*citing Kurtin v. KRE, LLC*, 2005 WL 1200188, at *3 (Del. Ch. 2005)
[30] *Id*. (*citing New Castle County v. Acierno*, 1995 WL 694426 (Del. Ch. Oct. 19, 1995)

Courts have altered the traditional approach of looking to the complaints' timestamps and begun looking at other factors to help determine if an action is entitled to "first filed" status.[31] These additional factors are: (1) the quality and substance of the complaint, (2) the representative nature of the party filing the action[32] and (3) whether the action presents novel issues concerning Delaware law.

The Delaware Chancery Courts have stated that the purposes behind these additional factors are based on considerations of trying to avoid: (1) encouraging the shoddy work of attorneys who hastily draft complaints—ultimately detracting from the best interests of the class they are purporting to represent;[33] (2) applying too much weight to "first filed" status (thus unfairly prejudicing one party);[34] and (3) the potential divergence between lawyers' best interests and the shareholders' best interests[35]

After considering these additional factors in light of the facts and circumstances of this case, a *McWane* analysis is still appropriate in determining whether to stay the proceedings in Delaware.

1. The Quality and Substance of the Complaint

The first factor, the quality and substance of the complaint, weighs in favor of the Texas complaint. The Delaware action was copied, nearly

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[31] *Rosen v. Wind River Systems, Inc*., C.A. No. 4674-VCP (Del. Ch. 2009); *See also In re IBP, Inc. S'holders Litig*., 2001 WL 406292, at *8 (Del. Ch. 2001)

[32] *Id*.

[33] *In re Topps Co. S'holder Litig*., 924 A.2d 951, 957 (Del. Ch. 2007) *See also Biondi v. Scrushy,* 820 A.2d 1148, 1162 (Del. Ch. 2003) (Stating "Delaware law places more emphasis on quality than speed when assessing derivative complaints.")

[34] *In re IBP, Inc. S'holders Litig*., 2001 WL 406292, at *8 (Del. Ch. 2001) (Stating that, "[to] call an action filed five hours previously a "prior pending" one and thereby avoid a genuine inquiry into where the parties' dispute should be heard would sacrifice reason for the sake of a bright-line rule of questionable efficiency and justice")

[35] *Biondi*, 820 A.2d at 1159

verbatim, from the complaint filed in the Texas action. Therefore it could not be argued that either complaint was better drafted, as they are nearly identical. Arguably, the Delaware complaint should warrant less respect and deference and is facially indicative of the haste and lack of merit that this factor is designed to prevent.

The Delaware complaint was most likely prepared and filed simply as a tactic to defeat Mr. Miller's choice of forum. This Court should not honor the Delaware plaintiffs' attempt to defeat the first-filed status of Plaintiff Miller's action simply by filing a nearly identical copy of the Texas complaint with this Court.

2. Delaware Courts Give Less Deference to Plaintiff's Choice of Forum in Representative Actions

The second factor to consider, that Delaware Courts give less deference to a Plaintiff's choice of forum in representative actions, should be considered lightly by this Court. This is particularly evident where none of the transgressions exist that the consideration of this factor are designed to address.

When a foreign action is first filed by a **derivative suit** plaintiff, the Court in *Biondi* stated that Delaware Courts should "place less emphasis on the celerity of such plaintiffs and grant less deference to the speedy plaintiff's choice of forum." The Court reasoned that this lack of deference was necessary because of the "potential divergence in the best interests of the plaintiffs' attorneys and the plaintiffs they are purporting to represent" and, further, that this divergence "may be exacerbated by a legal rule that places determinative weight on which complaint was filed first."[36] As mentioned above, Delaware Courts have stated that allowing first-filed

[36] *Biondi*, 820 A.2d at 1159

status to be determinative would promote sub-par lawyering as each attorney would hastily draft his or her complaint in a "race to the courthouse."

Under the facts of the current case however, this is not the situation. The *Biondi* Court recognized that although the above dangers exist, "there is utility to a legal rule of decision that promotes comity and judicial economy by reducing the likelihood for duplicative effort and unseemly wrestling over which forum should take hold of a matter."[37]

Without considering the first-filed status of a case where the facts warrant such a consideration, Delaware Courts and the public would be hard-pressed to establish a cognizable, objective foundation upon which to analyze the propriety of a forum for litigation. This could lead to costly, duplicative litigation and judicial "turf wars" over which forum is appropriate.[38] Thus, by not appealing to some sort of objective standard Delaware Courts would ill-serve the twin principles of comity and judicial economy that are touted as the two primary goals behind any Motion to Stay Proceedings analysis.[39]

Plaintiff Miller filed the first action in Texas. The events that led up to this derivative suit, the directors, the witnesses, Pinpoints headquarters and all of the main parties involved in this action hail from Texas. It is logical to bring suit in Texas. This is not the case of a hasty attorney initiating an action in a far-flung jurisdiction seeking to leverage a foreign court's law and authority over a transaction that it has attenuated connections with.

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[37] *Biondi*, 820 A.2d at 1158-59

[38] *See* Stevelman, Faith, *Regulatory Competition, Choice of Forum, and Delaware's Stake in Corporate Law* (2009)

[39] *Mine Safety Appliances Co. v. AIU Ins. Co*., 2011 WL 300252, at *4 (Del.Super. 2011) (*citing Palmer v. Palmer*, 409 A.2d 1050, 1051 (Del. 1979)) (When dealing with parallel proceedings the "Court's primary goals… are to maximize the economy of judicial effort and the efficiency of the administration of justice.")

As far as the time of filing is concerned, although Plaintiff Miller filed suit a day after the settlement announcement—he did so on an informed basis with the necessary information. It could not be said that the derivative plaintiffs from Delaware are any more deserving of deference or even entitled to have this Court take a less favorable view of the Texas action as compared to the Delaware action.

Therefore this factor should have little if any bearing on this Court's decision on the applicability of a *McWane* analysis.

3. Actions Addressing Novel Issues of Delaware Law

The third factor, whether the action addresses novel issues of Delaware law, must also weigh in favor of the Texas action. There are currently no pending novel issues of Delaware law in this litigation (absent the bylaw adoption which this Court is to decide). The only claim being addressed is a common law breach of fiduciary duty claim for lack of oversight and loyalty. These claims do not implicate any novel issues of Delaware corporate law.

Further, Delaware Courts have "recognized without hesitation that sister state courts and federal courts are capable of applying Delaware law and providing complete justice to parties."[40] This should have even stronger bearing when these foreign courts are not addressing any complex or novel issues of Delaware law, but an issue that is commonplace and well-decided in Delaware litigation.

Ultimately Delaware Courts hope to avoid the inequities that may arise from giving blind deference to the choice of forum of whichever party "won the race to the courthouse" without a genuine consideration of which forum would be most proper.[41] The three transgressions that are sought to be avoided: (1) sub-par lawyering, (2) unwarranted, possibly prejudicial deference to the

[40] *In re Westell Techs., Inc*., 2001 WL 755134 (Del.Ch. June 28, 2001)
[41] *In re IBP, Inc. S'holders Litig*., 2001 WL 406292, at *8 (Del. Ch. 2001)

first-filer's choice of forum and (3) a divergence in best interests of the lawyers and shareholders are simply not taking place in the current action.

There is no dispute that Plaintiff Miller filed the Texas action first. Further the complaint is not the product of haste or bad lawyering—and it has not been formally recognized as such by either the Court of Chancery, nor explicitly stated by the Defendants.[42] Further, the "photocopied" complaint was filed in Delaware by other Pinpoint shareholders for the sole purpose of defeating Plaintiff Miller's choice of forum. If anything, this conduct implicates all three of the transgressions that are sought to be avoided: sub-par lawyering, a race to the courthouse, and using "filing tactics" to decide the propriety of a forum.

It is therefore the contention of Plaintiff Miller that this Court not recognize the Delaware Plaintiffs' forum-defeating tactics as a legitimate, contemporaneously filed action; that his complaint be entitled to first-filed status; and that as such the Motion to Stay Proceedings should be decided under a *McWane* analysis.

C. Under the McWane Doctrine the Delaware Proceedings Should be Stayed in Favor of the Proceedings in Texas

Under a *McWane* analysis it is indisputable that the facts of this case warrant a stay of the Delaware proceedings in favor of the proceedings in Texas. "[A]s a general rule, litigation should be confined to the forum in which it is first commenced, and a defendant should not be permitted to defeat the plaintiff's choice of forum in a pending suit by commencing litigation involving the same cause of action in another jurisdiction of its own choosing."[43]

"Accordingly, the Court's discretion 'should be exercised freely in favor of the stay' when: (1) there is a prior pending action in another

[42] However Defendants have filed a Motion to Dismiss Plaintiff Miller's complaint.
[43] *McWane*, 263 A.2d at 283

jurisdiction; (2) that involves the same parties and issues; and (3) the other jurisdiction's courts are capable of delivering prompt and complete justice."[44] The Court will "balance these factors and all other pertinent facts and circumstances against the possibility of inconsistent and conflicting rulings if both actions are permitted to proceed at the same time."[45]

All three of the factors enumerated above exist in the current case and are wholly uncontested. There is (1) a prior pending action in the United States District Court for the Southern District of Texas, (2) the exact same parties and issues are involved in that case and (3) the District Court in Texas is a court of competent jurisdiction capable of effectuating prompt and complete justice.

When balancing the above factors with the possibility of duplicative litigation and inconsistent rulings courts should, "in the interests of comity and judicial economy…stay [the] after-filed suit in Delaware [where] a previously filed suit stating similar claims is pending in a court of another state."[46] To allow this Delaware action to continue under the current circumstances, while an identical action is pending in the United States District Court for the Southern District of Texas would be inequitable and create the possibility of inconsistent and conflicting rulings and "[t]hat is precisely the outcome *McWane's* doctrine of comity seeks to prevent."[47]

D. The Proceedings in Delaware Should Also be Stayed Under a Forum Non Conveniens Analysis

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[44] *Id*. (*citing McWane*, 263 A.2d at 283)
[45] *Id*.
[46] *Transamerica Corp. v. Reliance Ins. Co. of Ill*., 1995 WL 1312656, at *3 (Del. Super.) (*citing McWane*, 263 A.2d at 283.)
[47] *LISA, SA v. Mayorga*, 993 A. 2d 1042, 1048 (Del. 2010)

If the court finds the above argument unpersuasive and determines that both actions were filed contemporaneously, Plaintiff Miller asserts that the Motion to Stay Proceedings in Delaware should still be granted under a *Forum Non Conveniens* analysis.

"When a shareholder brings a derivative action in the State of incorporation after another shareholder has filed an identical or similar action in another State, a court proceeds cautiously when faced with the question of whether to defer to a first filed representative suit, examining more closely the relevant factors bearing on where the case should best proceed, using something akin to a *forum non conveniens* analysis."

In order for a party to prevail on a Motion to Stay under a *Forum Non Conveniens* analysis, that party must show that the traditional *Forum Non Conveniens* factors weigh so heavily against suit in Delaware that party seeking the Motion to Stay would suffer an overwhelming hardship should it be forced to litigate in Delaware.[48]

When deciding a Motion to Stay under a traditional *Forum Non Conveniens* analysis, the Delaware Supreme Court has identified the following as factors (known as the *Cryo-Maid* factors) to be considered:

> (1) the relative ease of access to proof;
> (2) the availability of compulsory process for witnesses;
> (3) the possibility of the view of the premises;
> (4) whether the controversy is dependent upon the application of Delaware law which the courts of this State more properly should decide than those of another jurisdiction;
> (5) the pendency or nonpendency of a similar action or actions in another jurisdiction; and
> (6) all other practical problems that would make the trial of the case easy, expeditious and inexpensive.[49]

The factors above provide only a framework in assessing whether a party will suffer an overwhelming hardship if forced to litigate in Delaware. No

[48] *Williams Gas Supply Co. v. Apache Corp.*, 594 A.2d 34, 37 (Del.1991)
[49] *Taylor v. LSI Logic Corp.*, 689 A.2d 1196, 1198-99 (Del. 1997).

single factor is determinative in the outcome—it does not matter whether one factor establishes the overwhelming hardship or that all of the factors cumulatively do.[50] "The issue is whether **any** or **all** of the Cryo-Maid factors establish that [the party] will suffer overwhelming hardship and inconvenience if forced to litigate in Delaware."

Factors (1), (5) and (6) are the only factors necessary to establish overwhelming hardship in the current case[51]. Factor (1) addresses the *relative ease of access to proof*. Although not determinative by itself, the fact that all of the relevant events transpired in Texas and also that the company headquarters, directors, evidence and witnesses are all located in Texas show some degree of hardship, albeit not overwhelming hardship.

Factors (5) *the pendency of a similar action in another jurisdiction* and (6) *practical problems that would make the trial of the case easy, expeditious and inexpensive* establish the necessary circumstances to show that Plaintiff Miller, individually **and** as representative for the company (as plaintiffs in derivative suits are recognized as mere "surrogates" bringing suit on behalf of the company[52])would suffer overwhelming hardship. There is a pending federal claim in the Texas District Court which will not be dismissed, as at least one claim against the company is based on the violation of federal securities law. As such, if this Court does not stay the current action, the company will definitively be forced to litigate in two different forums which are thousands of miles apart. As the Court of Chancery recognized in the current action, "the [directors]… envision concurrent litigation in which the exclusively federal law claims would proceed in the Federal Action in Texas while the Delaware state law

[50] *Id*. (emphasis added)
[51] With factors (5) and (6) being able to establish overwhelming hardship by themselves.
[52] *Topps*, 924 A.2d at 957 (Del. Ch. 2007); *See also Koster v. Lumbermens Mutual Casualty Co.,* 330 U.S. 518 (1947)

derivative claims would proceed in this Court."[53] This is not only financially burdensome, but extremely impractical—almost to the point that neither claim could be adequately litigated.

Failure to stay the proceedings in the Delaware action could also have the effect of forcing the company to not only litigate the federal claim in Texas and the state claim in Delaware, but also litigate the state claim in Texas as well. This is in light of a recent California federal court decision refusing to stay proceedings in an action **identical** to this one. This prior ruling could be indicative of a possible decision coming out of Texas on the motion to stay proceedings that is pending before it, where Texas may decide that it is proper and indeed necessary that the state law claims be litigated in Texas.

Although the *Forum Non Conveniens* analysis is not a balancing test[54]; the Court should take notice of the possible implications of its decisional alternatives. First, the Court could stay the Delaware proceedings in favor of the Texas proceedings, forcing the directors to litigate all claims in the company and directors' home state of Texas which is also where all the events relevant to this action took place. Alternatively, the Court could refuse to stay proceedings in Delaware. In such a scenario the company would be forced to litigate (for all practical purposes) the same problem on a state level in Delaware and a Federal level in Texas and may further even have to litigate the state claim in the Texas federal court as well, should the court refuse to stay proceedings on the state law claim.

The impracticability and possible impossibility of litigating three identical claims in separate courts, the financial waste it will cause Miller and the company, and the possibility of inconsistent judgments should

[53] (R. at 8.)
[54] *Aveta, Inc. v. Colon*, 942 A.2d 603, 607 n.7 (Del. Ch. 2008)

evidence the "overwhelming hardship" that both the company and Plaintiff Miller will face if this Court refuses to stay the proceedings in Delaware in favor of the proceedings in Texas.

Indeed, the Supreme Court of the United States further touched on this exact issue stating that under a *Forum Non Conveniens* analysis, "the ultimate inquiry is where trial will best serve the convenience of the parties and the ends of justice."[55] The Supreme Court went on to state that,

> Under modern conditions corporations often obtain their charters from states where they no more than maintain an agent to comply with local requirements, while every other activity is conducted far from the chartering state. Place of [incorporation] in such circumstances might be entitled to little consideration under the doctrine of forum non conveniens, which resists formalization and looks to the realities that make for doing justice.[56]

It is for the above reasons that Plaintiff Miller believes he will suffer "overwhelming hardship" should he be forced to litigate in Delaware. Plaintiff Miller further states that it would be for the convenience of the parties and in the interests of justice that this action be stayed in favor of the proceedings in Texas.

CONCLUSION

For the aforementioned reasons, Mr. Miller respectfully requests that the Delaware Supreme Court find the exclusive forum bylaw invalid and further allow him to litigate this case in Texas.

February 11, 2011

Respectfully Submitted

Team X

Counsel for Appellant

[55] *Koster*, 330 U.S. at 527 (1947)

[56] *Id*. at 527-528.